

Contract Law in Malaysia: Reflections on Its Ideologies and Concepts

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ABSTRACT

In tracing the development of law of contract in Malaysia, the article examines and discusses the ideologies and concepts that have been responsible in shaping and molding the law of contract in Malaysia and in its legal system. To achieve these objectives, the social, philosophical, economic and political thoughts and values that have influenced the law have been analyzed. A brief discussion on the current trend of the law is also included.

Keywords: *political entity, legislature, judiciary, paternalistic traditions*

Undang-Undang Kontrak di Malaysia: Penterjemahan ke atas Ideologi dan Konsep

ABSTRAK

Dalam usaha untuk meneliti pembangunan dalam undang-undang kontrak di Malaysia, artikel ini mengkaji dan membincangkan ideologi dan konsep yang telah bertanggung jawab untuk membentuk dan menggarapkan undang-undang kontrak di Malaysia serta sistem perundangannya. Untuk mencapai objektif tersebut, pemikiran dan nilai-nilai sosial, filosofi, ekonomi dan politik yang telah mempengaruhi undang-undang telah dianalisis. Perbincangan ringkas mengenai tren undang-undang masakini juga disertakan.

Katakunci: *entiti politik, perundangan, judisiari, tradisi paternalistik*

INTRODUCTION

Prior to the advent of the British, there had been some sort of judicial system in existence in the various places that are now called Malaysia. In each Malay state there was a separate political entity with its own ruler, legislature and judiciary. The sultans were the sovereign rulers in whom resided all legislative and executive power. Administration of justice was the responsibility of the *Bendahara*, the *Temenggong* and the *Laksamana*.¹ As the law was based on customary law (with the relic of Hindu law overlaid by Islamic law), it was thus governed by paternalistic traditions that were mainly patriarchal in nature. In “Undang-undang Melaka” (a digest of law on Malacca), for example, it has been stated that the jurisdiction of this digest covered, “all larged lands and by all great rulers and their viziers and on the customs in the dependent areas and village.”² The paternalistic character was reflected in the law of this digest which governed the responsibilities of the ruler and his chiefs, prohibitions amongst members of the community, penalties for criminal and civil offences, family law and other matters.³ As such, the role of the individual was quite limited and to some extent appeared to be insignificant. This may also be because of the strict application of “autocratic” patriarchal customary law which demand total respect and loyalty to the rulers, the chiefs, the head of the family or the elders. Thus, any form of excessive individual freedom, such as the right of rebellion or the right to express one’s feeling may be interpreted as an act of disrespect or disloyal to the rulers, the chiefs, the head of the family or the elders.⁴

However, the beginning of the nineteenth century witnessed some development in Malaysian legal system. During this colonial era, the British had introduced Western administration in the country, *“the most important aspect of which was the effecting of British laws without, however, totally obliterating indigenous laws (especially with regard to land administration) and Islamic law.”*⁵ Indeed, English law was adopted only so far as it was suitable to local conditions. In some instances, it was adopted indirectly and without statutory authority through the judiciary applying English legal principles to cases that came before them for determination.⁶ In others, statutory authority including the Royal Charters of Justice⁷ provided for the introduction of English law that were suitable to local conditions in the absence of local laws. This eventually led to “the introduction of the democratic process leading in 1957 to the establishment of parliamentary democracy- with a written constitution, a House of Representatives (to which members are elected based on universal suffrage) and a Senate. In the process, the Malay Kingdoms were first united into a nation.”⁸

The colonial era also witnessed major economic transformation which is described by Prof. Khoo Kay Kim⁹ as follows:

“The early 19th century marked the beginning of an economy anchored to the export of raw materials. Tin production though not new expanded radically in response to Britain’s growing tin-plate industry; commercial agriculture, a new phenomenon, assumed increasingly greater importance; and the development of infrastructure to meet the needs of the new economy took off by the 1800s (railway, urbanization with all its ramifications, and road transport being the most important until World War 1)”.

What ensued from this was the development of law in the area of commercial law. In 1878, for example, by virtue of section 6 of the Civil Law Ordinance 1878, English commercial law was introduced into the Straits Settlements.¹⁰ It then became clear that English law relating to contracts was applicable to Penang, Malacca and Singapore.¹¹ Similarly, by 1899, the Contract Enactment which was modelled on the Indian Contract Act 1872 (that was based on the English principles) was extended to the four states of the Federated Malay States. This Enactment of 1899 was then gradually extended to the Unfederated Malay States, with Johore as the first state to accept its application, as early as 1914.

Freedom of Contract Ideology as Reflected in the Contracts Act 1950

The oldest printed version of the provisions relating to contracts is the Contract Enactment 1899. However, it was not formally passed by the Federal Legislative Council of the Federation of Malaya until 1950. The Contract Ordinance 1950 was then revised in 1974 and it became an Act by virtue of the Revision of Laws Act 1968.

The Malaysian Contracts Act 1950 has its forbear in the Indian Contract Act 1872, thus, naturally the provisions contained in the Act reflect the English model of contract theory of the nineteenth century which was closely related to the development of the free market and the ideals of classical economics. In other words, the 1950 Act would be based on the then prevailing judicial philosophy of *laissez-faire* based on the conception of the rugged individualist. Indeed, this was judicially recognised by the Privy Council in the Malaysian case of *Ooi Boon Leong & Ors v Citibank N A*.¹² The main legal issue in this case was whether the parties to a contract can contract out of the provisions of the Contracts Act 1950. The Privy Council, in allowing the parties concerned to contract out of the provisions of the Contracts Act, referred to section 1(2) of the Act¹³ which was strongly relied by the appellants in this case.

“Section 1(2) has no effect on the freedom of contracting parties to decide upon what terms they desire to

contract. It would be indeed surprising if so devastating an inroad into the common law right of freedom of contract were introduced by the legislature in a section which is primarily devoted to expressing the short title to the Act and which moreover appear in a part of the Act which is merely headed ‘Preliminary’.”¹⁴

In a similar vein, the Privy Council further observed:

“Random recognition in certain sections of the Act of the fundamental principle that contracting parties are at liberty to express their intentions in their contracts as they please is quite insufficient to support the contrary proposition that the absence of such recognition in another section implies the absence of freedom of contract. If freedom of contract is to be curtailed in relation to a particular subject matter, their Lordships would expect the prohibition to be expressed in the statute, and not left by the legislature to be picked up by the reader as an implication based upon sections dealing with different subject matters.”¹⁵

It is significant that the Privy Council in this case emphasized the principle of freedom of contract as being paramount in the judicial consideration of the operation of the Contracts Act. Thus, the above observations illustrate that according to the Privy Council the doctrine of freedom of contract is the superstructure upon which the Contracts Act, 1950 is built. It is also quite apparent that the notion of individual liberty emphasized in the above quoted passage reflects the influence of the will theory on the law of contract.

Indeed, the central theme of the freedom of contract doctrine is the individual and the choice that he has freely made. This theme appears to be so embedded in the provisions of the Contracts Act 1950 that section 10 of the Act defines contracts as, “*all agreements made with the free consent of parties competent to contract..*”.

Hence, the foundation of legal liability is the consent of both parties, freely given, to be bound by their agreement. Factors which vitiate such consent, for example, undue influence, fraud, misrepresentation and certain categories of mistake¹⁶ are simply illustrations of defective consent or unfree will which render the resulting agreement voidable. The Contract Act’s obsession with free consent is explained by Noor Alam¹⁷ as being:

“...deeply rooted in the assumption of the freedom of contract doctrine that every individual is equally capable of making a rational choice. Once that choice has been made, the law will not go behind it to enquire into the social and environmental setting that influence the choice and render its ‘free’ characteristic merely illusory.”

Clearly, the Contracts Act has fostered the idea of freedom of contract and adopted an objective view of agreement which makes the law more concerned with the procedural aspect of fairness rather than the substantive fairness of a transaction. This characteristic of nineteenth century ideology of law is reflected in the general principles embodied in the provisions of the Act, which will be discussed below.

Firstly, as in the classical contract theory, the Contracts Act emphasizes the rule of offer and acceptance. An agreement arrived at through the mechanism of offer and acceptance is regarded as a manifestation of the meeting minds of the parties.¹⁸ Secondly, neither party owes any duty to volunteer information to the other, thus as the *Explanation* to section 17 of the Act¹⁹ provides, “*Mere silence as to facts likely to affect the willingness of a person to enter into a contract is not fraud.*” This is merely a restatement of the common law. It is only if, “*the circumstances of the case are such that, ... it is the duty of the person keeping silence to speak, or unless his silence is, in itself, equivalent to speech*” that the other party is

entitled to rely upon them.

Nevertheless, the one significant difference is that, under the Contract Act, the misrepresentation or silence which is fraudulent in the context of section 17 will not render the contract voidable if the other party whose consent was caused by that misrepresentation or fraudulent silence had the means of discovering the truth with ordinary diligence. Thirdly, the emphasis on contract law as the law of the market is also reflected in the narrow application of the doctrine of mistake under the Contracts Act. Under section 23, for instance, parties will not be easily discharged from their contractual undertakings simply because they entered into the contract under some mistake. As under the classical contract theory, the Contract Act takes a predominantly objective view of agreement. Thus, *“an erroneous opinion as to the value of the thing which forms the subject-matter of the agreement is not to be deemed a mistake”*.²⁰ It is not, in general, the subjective intention of the parties with which the Act is concerned, but rather what can be inferred from their conduct. Finally, the concept of freedom of contract being the foundation of the Contracts Act 1950 is further emphasised by the fact that the Act contains a provision which renders all contracts in restraint of trade void (subject to the limited exceptions).²¹ The object of this provision appears to be protecting the public interest, in particular to prevent monopoly of business, trade and profession which seemed appropriate during the nineteenth century as the economy was only beginning to develop.

From what was mentioned above, all these rules can probably be rationalised in terms of the underlying doctrine of freedom of contract in the Contracts Act. Where both parties are of full age, fully competent to negotiate a deal and to take the necessary and ordinary precautions, the law will not intervene to correct any imbalance in the exchange or bargain which has been agreed upon by the parties. In the interests of certainty and commercial convenience, parties are bound by their apparent agreement. Nevertheless, although the Contracts Act fostered the ideology of freedom of contract in most of its provisions, there are, however, some provisions that restrict the freedom of the parties to contract, for example, those dealing with contracts which are illegal, immoral or against public policy or agreements, which contravene any statutory law.²²

State Intervention

Apart from the Contracts Act 1950, which fostered the idea of freedom of contract, the movement towards economic liberalism had never quite made any significant impact in social, economic and legal aspects of life in theory and practice in Malaysia. This may be partly because of the strict application of autocratic patriarchal customary law that had been in practiced throughout the eighteenth and nineteenth century which to a certain extent restricted individual freedom and his right of choice. Whatever freedom a man desire had to be within the limit of the customary law and according to the prevailing views in the community of what was right and wrong. Apart from this, Malaysia too had never experienced a revolution such as the Industrial Revolution that took place in England which began around the middle of the eighteenth century. Hence, the effect of such an experience was less effective here in Malaysia and it had not influenced any significant change in the system.

Furthermore, the failure of the free market to conform with the social and economic reality which led to monopoly and concentration of trade and industries in England, might also hinder the development of this movement in Malaysia. The fact that the market economy could no longer accorded with the reality of the modern world could have made the ideology of economic liberalism seems fallacy to Malaysian economist.

In modern Malaysia, it will be observed that since independence²³ the government of Malaysia²⁴ does not seem to favour the free market ideology. This is evident from the government's direct involvement in the Malaysian economy. Most of the public enterprises at the time of independence were controlled by the

government and although at the beginning they were engaged in traditional activities associated with public utilities, transportation, communication, agriculture development and finance, it had since then been extended to the manufacturing and service sectors.²⁵ The rapid expansion of public enterprises could be seen, in particular, in the 1970s-1980s. The government believes that such direct involvement in economy is necessary in order to promote social-economic development. It is also to foster racial harmony in Malaysia - by balancing the wealth and advantage between the Malay and non-Malays.²⁶ A reflection of this belief is noted by Ghazali Yusoff²⁷ when he discusses racial harmony in Malaysia: “since independence, the government has recognized that economic inequalities could provide “flashpoint” in society. Such an occurrence did take place in 1969 and a pragmatic and affirmative social engineering programme was introduced - the New Economic Policy (NEP)²⁸ - to review the balance of wealth between the Malays and non-Malays. This engineering continues till today and it has taken place with little traumatic responses from the other races.”

At this juncture, perhaps it ought to be pointed out that the Malaysian government’s economic policy appears, to some extent, to resemble the collectivistic policy. Collectivism was concerned about equalities and the protection of the weak against the strong. To them, state help and intervention were necessary in order to help balance the inequalities of wealth and distribution of the national production among the people. Thus, both collectivism and the Malaysian government’s economic policy seem to be based on the same ground, that is, the faith in the mass of people and the benefit which they will receive by the action of the state, or its intervention even in the private sector if necessary.

State intervention can also be seen in many government regulations that intervene with private contractual relationship. This is reflected, for example, in relation to insurance and employment contracts by the Insurance Act 1965 and the Road Traffic Act 1958 which dictate many of the terms of insurance contracts, and the Employment (Termination and Lay-off Benefits) Regulations, 1980 which deal with an employer’s liability for termination and lay-off benefits in employment contracts. However, state intervention in consumer protection legislation is quite minimal in Malaysia. This in part is due to the limited acceptance of laissez-faire. Nevertheless, some statutes do exist which, to some degree, indicate state intervention in private contractual relationships. For example, the Sale of Goods Act 1957, the Hire-Purchase Act 1967 and the National Land Code 1965 which specifically provide that certain terms are to be implied into particular contracts. Of a similar effect is the Moneylenders Act 1951 which involves some interventions in the express terms of contracts for consumer credit. In addition, the government’s interest in consumer protection has recently been renewed with the enactment of the Consumer Protection Act 1999 which, it is claimed, to be the first comprehensive protection Act in Malaysia.

State intervention is also reflected in the administration of Muslim law in the country. For example, in each state, Islamic law is administered according to the Administration of Muslim Law Enactments or Ordinances.²⁹ These Enactments are similar in content and they mainly govern the laws concerning marriage and divorce, maintenance of dependants, guardianship or custody of infants among Muslims. Recently, Islamic tenets have been extended into other areas such as banking and insurance law which is governed by the Islamic Banking Act. This is the government’s attempt to merge religious practices with business law. Although these banking and insurance systems are offered to Muslim and non-Muslim customers, the laws are only applicable to those who opt for them.

Nevertheless, it is necessary to point out here that although the government’s presence can be felt in most of the economic, social and legal aspects of life in Malaysia, recently there has been an attempt to reduce its size and presence in the economy and to allow market forces to govern economic activities. This is reflected in the privatisation policy which was introduced in 1983. “It made explicit that excessive government’s presence in the economy be reduced, while emphasizing an increasing role by the private sector. The factors underlying this change signalled the Malaysian government’s intent to realign the

balance between the public and private sector's responsibilities",³⁰ and it also complements other national policies such as "Malaysia Incorporated",³¹ formulated to further strengthen the role of the private sector as the engine in the economy. However, it is still not clear to what extent these pragmatic approaches will affect the government's ideology. But today, privatisation is increasingly being expanded by the government through government-owned enterprises as well as new projects.

External Influences Affecting Malaysian Contract Law

The evolution of new doctrines and approaches in English law such as economic duress, inequality of bargaining power and the broader doctrine of unconscionability has to a certain degree influenced the development of Malaysian contract law. Although the Contracts Act does not incorporate such principles as economic duress, inequality of bargaining power or unconscionability as have recently been developed in English law, there is some evidence to indicate that such principles are judicially recognised in Malaysia. The courts have dealt with such issues although their status and application are still a matter of debate. However, it is beyond the scope of this paper to examine the matter in depth. Suffice to mention here that, this does not mean that the Malaysian courts will blindly adopt all the new doctrines that have been developed by the English law. Any doctrines or approaches which do not accord with the moral standards of the society or which contravene public policy will not be accepted by the Malaysian courts. This was made clear by the Court of Appeal in the recent case of *Tengku Abdullah Ibni Sultan Abu Bakar Mohd Latiff & Ors*³², when it refused to extend the doctrine of undue influence to non-marital relationships on grounds of public policy. The decision in this case illustrates that the courts recognised the right to modify principles of the common law and doctrines of equity that have their historical origins in England to suit the domestic needs of the Malaysian jurisdiction.

CONCLUSION

As will be apparent from the above discussion, the significance of the role played by an individualist society in the development of modern English contract law can scarcely be denied. Indeed, the origin and, to a large extent, the heyday of modern contract law began in the period of individualism where the emphasis upon freedom of choice, the value of a free market economy and a less paternalistic role for the state were associated with the classical law of contract. As Wheeler³³ observes, "the modern paradigm of contract owes much to what is often termed the 'classical law of contract', a body of rules principally formulated in the nineteenth century, in the search to set out a coherent and consistent operating framework for the exercise of private autonomy through agreement." However, because of the failure of individualism, the classical theory of contract has less relevance today.

In turn, the interventionist approach "paternalism" is now seen as a legitimate function of the law. There is formal acknowledgement that certain contracting parties need the protection of the law against economic exploitation and oppression. Contract law is changing to reflect these changes in economic reality.

In Malaysia, the growth and development of the classical model of contract naturally produced a profound impact on the Malaysian Contracts Act 1950. As noted earlier, this classical theory of contract law is mirrored in most of the provisions embodied in the Act. But apart from the 1950 Act, it is probably fair to say that the classical theory has played a less significant role over human affairs and conduct in Malaysia. A relatively excessive interventionist approach adopted by the government has inevitably restricted the growth of this theory. As a result, some degree of paternalism can be felt in the government's regulations, policies and administrations. But this does not seem to hinder the development of contract law in Malaysia. Although the changing process is much slower than in England, it is evident

that the contract law in Malaysia is moving towards a significant change as in English law.

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ENDNOTES

- ¹ The power of the Bendahara could be equated with the power of the Prime Minister today, whilst the Temenggong had the power of a Chief of Police and the Laksamana had the power of an officer who executed the sentenced passed, aside from being the Commander-in-Chief.
² Liaw Yock Fang, *Undang-undang Melaka*, (1976) at 62.
³ See Muhammad Yusof Hashim, *Islam dalam Sejarah Perundangan Melaka [Islam in Malacca Legal History]* in *Islam di Malaysia*, Publication of History Association of Malaysia.
⁴ For general discussion see Yusoff Iskandar and Abd Rahman, *Sejarah Melayu, Satu Perbincangan Kritis dari Pelbagai Bidang*, [Sejarah Melayu, An analysis from various Aspect] (1978).
⁵ Prof. Khoo Kay Kim, “Malaysian Heritage and Culture: Past, Present and Future” in *Malaysia Today Towards The New Millennium* (1997) at 305-306.
⁶ Leonard Nachiappa Chetty (1923) 4 FMSLR 265; Haji Abdul Rahman Mohamed Hassan (1917) AC 206.
⁷ The first Charter of Justice was introduced in 1807, followed by the second and third Charters in 1826 and 1855 respectively.
⁸ Prof. Khoo Kay Kim, “Malaysia Heritage and Culture: Past, Present and Future” in *Malaysia Today Towards The New Millennium* (1997) at 306.
⁹ Ibid.
¹⁰ This provision is now found in section 5(2) of the Civil Law Act 1956 (Act 67) (Revised 1972).
¹¹ English law relating to contracts continued to apply to Penang and Malacca up to 1974, when Contracts Act was extended to these two states.

¹² Section 1(2) of the Contracts Act 1950 provides that: “Nothing herein contained shall effect any written law or any usage or custom of trade, or any incident of any contract, not inconsistent with this Act.”

¹³ Ibid at 226.

¹⁴ Ibid.

¹⁵ See section 14 of the Contracts Act 1950.

¹⁶ See Part II of the Contracts Act 1950, in particular sections 4-9.

¹⁷ Section 17 of the Contracts Act deals with the element of fraud.

¹⁸ See *Explanation* to section 21 of the Contracts Act 1950.

¹⁹ See for example Exceptions 1-3 of section 28 of the Contracts Act 1950.

²⁰ See for example section 24 (a) - (e) of the Contracts Act 1950.

²¹ Malaysia gained independence in 1957.

²² There has only been one government in Malaysia since independence, that is, the Barisan National and it has been in power for nearly 47 years now.

²³ For further study see Vijayakumari Kanapathy and Ismail Muhd Salleh, *Malaysia Economy: Selected Issues and Policy Directions* (1994) at 167.

²⁴ The majority population in Malaysia consists of Malay, Chinese and Indian.

²⁵ Ghazali Yusoff, “The Malaysian Concept of Multireligious and Racial Harmony” in *Malaysia Today Towards the New Millenium* (1997) at 316.

²⁶ In 1990, the New Economic Policy is replaced by the National Development Policy (NDP).

²⁷ See the Muslim Courts (Criminal Jurisdiction) Act 1965, as amended by the Muslim Courts (Criminal Jurisdiction) (Amendment) Act 1984 with effect from 1st January 1985.

²⁸ Ismail Muhd Salleh, “Privatisation and Deregulation in Malaysia: Progress, Problems and Prospects”, in Vijayakumari Kanapathy, *Malaysian Economy: Selected Issues and Policy Directions* (1994) at 165.

²⁹ The term “Malaysia Incorporated” is used to describe the special relationship the nation aspires to achieve between the public and private sectors as a means to mould the nation into an advance, affluent industrial society.

³⁰ [1996] 4 MLJ 331.

³¹ Wheeler, *Contract Law: Cases, Material and Commentary* (1996) at 52.